

April 28, 2020

Tracy Swallwell
Assistant Commissioner for Securities and Regulated Industries
Iowa Insurance Division
Two Ruan Center
601 Locust St., 4th Floor.
Des Moines, IA 50309

Dear Ms. Swallwell,

Morgan Stanley Smith Barney LLC (“Morgan Stanley”, “we”) appreciates the opportunity to comment on the Iowa Insurance Division’s (the “Division’s”) proposed rule 191-50.104(502) related to best interest obligations in the brokerage business (the “Proposal”).

As described below, while Morgan Stanley supports the Division’s goals of transparency and increased investor protection, we believe specific clarifications can address concerns with current language contained in the Proposal.

I. MORGAN STANLEY BACKGROUND INFORMATION

Morgan Stanley is a leading full-service global financial services firm.¹ Since our founding in 1935, Morgan Stanley has been a client-focused organization providing a range of financial services and advice to individuals, corporations and institutions. Our employee code of conduct stresses the primacy of client interests over those of the company or individual employees, and four “Core Values” guide our business approach, the first of which is “Putting Clients First.”²

Morgan Stanley’s wealth management division, Morgan Stanley Wealth Management (“Morgan Stanley”), has approximately 15,700 financial advisors throughout the United States, servicing approximately 3.2 million wealth management relationships with approximately \$2.5 trillion in client assets. As of April 2020, Morgan Stanley had approximately 14,000 client accounts in the State of Iowa representing over \$8.8 billion in client household assets. Morgan Stanley provides services through both brokerage accounts with transaction-based pricing (e.g., commissions, selling concessions), and investment advisory accounts where clients pay an annual fee based on the value of the assets in the account. In Iowa, clients hold approximately \$5.4 billion in investment advisory accounts.

¹ Morgan Stanley (NYSE: MS) is a global financial services firm that, through its subsidiaries and affiliates, provides products and services to a large and diversified group of clients, including corporations, governments, financial institutions and individuals. Morgan Stanley Smith Barney LLC (doing business as “Morgan Stanley Wealth Management”) is registered as a broker-dealer and investment adviser with the SEC and a member of FINRA, the NYSE, NYSE MKT LLC, and NASDAQ Stock Market.

² The remaining Core Values are “Doing the Right Thing,” “Leading with Exceptional Ideas,” and “Giving Back.”

II. REGULATION BEST INTEREST HAS ALREADY CREATED A HEIGHTENED STANDARD OF CARE FOR BROKER-DEALERS

As you are aware, on June 5, 2019 the Securities and Exchange Commission (“SEC”) released Regulation Best Interest (“Reg BI”). Reg BI developed a heightened standard of conduct for broker-dealers (“BDs”) by which BDs making a personalized recommendation to a retail customer in a brokerage account involving a securities transaction or an investment strategy must act in the client’s best interest, without placing its financial or other interest ahead of the client’s interest. In pertinent part, this obligation requires BDs to (1) disclose all material facts about the scope and terms of the relationship, including fees and costs associated with the client’s account, holdings, and transactions, and all material facts relating to conflicts of interest (2) exercise diligence, care, and skill, including understanding the risks, reward and costs associated with a recommendation and (3) mitigate under various circumstances, and eliminate in specific instances, conflicts of interest associated with the recommendation.

Reg BI has broad applicability in that it includes all retail customer accounts (including retirement accounts) and incorporates fiduciary principles by going well beyond FINRA’s suitability standard. It creates robust investor safeguards and allows investors to continue to receive advice through the brokerage structure, thus preserving investor choice and permitting BDs to continue to receive commissions for executing transactions.

Lastly, Reg BI has already had a profound impact on the manner in which firms are fulfilling their regulatory requirements. This includes: oversight procedures, compensation, legal and compliance considerations, supervisory processes and business, operational and product strategy.

III. THE PROPOSAL SHOULD BE DELAYED IN LIGHT OF COVID-19

The coronavirus, or Covid-19, has caused many firms to reassess their business continuity plans and implement emergency procedures. In light of the difficulties brought on by this new reality, we respectfully urge the Division to delay the Proposal at this time. In the next two (2) months Reg BI will be applicable to federally-registered BDs providing recommendations to retail clients located in Iowa. Through the implementation of Reg BI, residents in Iowa will be afforded safeguards until the Proposal is released.

IV. A SAFE HARBOR SHOULD BE CREATED FOR BROKER DEALERS IN COMPLIANCE WITH REGULATION BEST INTEREST

In the event the Division decides to proceed with the Proposal, we suggest adding language pertaining to BDs already in compliance with Reg. BI. We strongly support language in SIFMA’s comment letter to the Division which recommends adding the following to the Proposal:

“A broker-dealer, or its agent, who is fully compliant with Securities and Exchange Commission Regulation Best Interest (17 C.F.R. §240.15l-1), as amended, will be deemed to be compliant with the best interest obligation in sub-rule 191-50.104(2).”

As it relates to 191-50.104(502), we further suggest amending the Proposal by adopting Reg BI’s definition of a “retail customer” in lieu of “retail investor.” The SEC defined a “retail customer” as a “natural person, or the legal representative of such natural person, who receives a recommendation of any securities transaction or investment strategy involving securities from a broker dealer or agent and uses that recommendation primarily for personal, family, or household purposes.” Adhering to this definition will ensure consistency, promote transparency and reduce confusion in the minds of Iowa customers.

V. SECTION 50.104(3)a(5) IS TOO ONEROUS AND SHOULD BE ELIMINATED

Section 50.104(3)a(5) requires firms to document that clients have been “reasonably informed” of the basis of a recommendation, potential risks, rewards and costs, on a trade-by-trade basis. Although no doubt well-intentioned, this aspect of the Proposal is not contained in Reg BI and would potentially create significant compliance burdens and costs for the reasons mentioned above. For the avoidance of doubt, the Care Obligation under Reg BI requires that BDs consider risks, rewards and costs when making a recommendation, but it “does not require BDs to document the basis for a recommendation.”³ Thus, we respectfully ask that the Division consider eliminating this section in order to create uniformity with existing federal guidance.

IV. CONCLUSION

We respectfully urge the Division to revise the Proposal to ensure it reflects robust safeguards already promulgated under Reg BI. For the reasons mentioned above, those BDs in full compliance with Reg BI should be afforded the right to be deemed in compliance with the Proposal’s “best interest” sub-rule 191-50.104(502). Adding an overlapping regulatory regime could result in confusion and unintended consequences that would not serve the interests of Iowa investors. Lastly, we request that the Division delay the rule based on the current pandemic and clarify that Section 19-50.104 of the Proposal does not create any new private cause of action or right of rescission, as the SEC noted in the Adopting Release of Reg BI.⁴

We thank you for consideration of our comments.

Sincerely,

³ 84 FR 33378, available at: <https://www.federalregister.gov/documents/2019/07/12/2019-12164/regulation-best-interest-the-broker-dealer-standard-of-conduct>.

⁴ 84 FR 33327, available at: <https://www.federalregister.gov/documents/2019/07/12/2019-12164/regulation-best-interest-the-broker-dealer-standard-of-conduct>.

MORGAN STANLEY SMITH BARNEY LLC

By: _____Anne Tennant_____

Managing Director and General Counsel